

TO: Files

CC: San Diego Audit Committee

FROM: Willkie Farr & Gallagher LLP

RE: Interview of George Coleman Conrad on April 25, 2006

DATED: April 26, 2006

On April 25, 2006, Sharon Blaskey, Michael Schachter, and Michael Shapiro, in Willkie Farr & Gallagher LLP's capacity as counsel to the Audit Committee, interviewed by telephone former Deputy City Manager George Coleman Conrad. The interview was conducted at the City Administration Building, 202 C Street in San Diego, in a conference room on the third floor. Johnny Giang and Wendy So from KPMG also attended the interview. Mr. Conrad was not represented by counsel.

The following memorandum reflects my thoughts, impressions, and opinions regarding our meeting with George Coleman Conrad, and constitutes protected attorney work product. It is not, nor is it intended to be, a substantially verbatim record of the interview.

Warnings

Ms. Blaskey began the interview by explaining the circumstances and purpose of the City of San Diego's (the "City") creation of the Audit Committee, noting that information obtained during the course of the interview would be used, if relevant, in the Audit Committee's eventual report. Ms. Blaskey explained that Willkie does not represent Mr. Conrad and, thus, statements made during the interview are not covered by the attorney-client privilege. Nonetheless, we would be treating the information obtained during the interview as confidential, covered by the work-product privilege during the investigation, but any such privilege would likely be lost with the release of the Audit Committee's report. Ms. Blaskey asked that Mr. Conrad keep the contents of the interview confidential. Ms. Blaskey further explained that, if requested, we would provide information from the interview to the SEC, the U.S. Attorney's Office or the City's outside auditor, KPMG, so it is important that Mr. Conrad be accurate and truthful. Ms. Blaskey emphasized that Mr. Conrad should seek clarification of any question at any time. Mr. Conrad asked what "kinds of things" are being investigated by the Audit Committee. Ms. Blaskey stated that the Audit Committee is examining the City's compliance or lack thereof with the rate structure requirements of the State Water Resources Control Board and the City's receipt of grants and loans. She noted that while we are also interviewing witnesses regarding the pension system, she did not believe we would discuss pension issues with Mr. Conrad.

Background

Ms. Blaskey asked Mr. Conrad to discuss his professional background. Mr. Conrad stated that he got a B.A. and a law degree before beginning to work for the City of San Diego. He worked for the City of San Diego from 1968 to 1997. During that time, he took a year off to practice administrative law in a private practice a law firm from 1977 to 1978; and took a sabbatical from September 1995 until October 1996. He became Deputy City Manager in 1978. In that position, several departments reported to him including Fire, Library, and the City Treasurer. Beginning in July 1995, the Metropolitan Wastewater Department became part of his responsibilities, after Roger Frondfedler, the Deputy City Manager who previously oversaw it, retired. Jack McGrory, City Manager, assigned him to the water and wastewater departments. As Deputy City Manager in 1995, he was responsible for six departments including Water, Sewer, Engineering, Environmental Services, Real Estate Assets, and General Services. He was responsible for general management and responded to the City Council on issues that arose regarding these six departments. Each department director reported to him: Frank Bellock (Engineering), Rich Hayes (Environmental Services), Cruz Gonzalez (General Services), David Schlesinger (Wastewater), George Loveland (Water), and Bob Collins (Real Estate Assets). George Loveland took over Conrad's responsibilities when he retired.

Ms. Blaskey asked Mr. Conrad about his responsibilities regarding the City Council. He said that he served in a liaison function, bringing issues before the Council or working on issues initiated by the Council. He would meet with Council staff and provide them with the facts regarding the issues. These meetings, which occurred daily, were arranged after he would receive requests from the Council staff to meet.

Knowledge of Sewer Issues

Ms. Blaskey asked Mr. Conrad about how sewer rates needed to be set in 1995-1996. Mr. Conrad stated that he did not know. Ms. Blaskey asked Mr. Conrad if he recalled a sewer rate issue coming before the Council in that time period. He did not recall, but did recall that a water rate issue went before Council. Ms. Blaskey asked Mr. Conrad if he was aware of grant and loan obligations related to the City's receipt of sewer funds for capital improvement projects. He stated that he was aware that San Diego received Federal and State funds for improvement projects but did not recall any discussion regarding obligations associated with receiving such funds. Ms. Blaskey asked Mr. Conrad if he is familiar with a Cost of Service Study ("COSS"), and he said he was familiar with the term. He said that the COSS's recommendations are determined by looking at the total costs of the system and calculating costs so that people are treated "equitably." He did not know if there were legal requirements involved and he did not deal with the rate structure. Ms. Blaskey asked Mr. Conrad if whether the sewer rate structure were to become a policy issue, he would have responsibility over it. He said he would have expected it to come to him.

Ms. Blaskey asked Mr. Conrad if he was familiar with the requirements to allocate costs based on the parameters of SS (Suspended Solids), flow, and BOD (Biological Oxygen Demand)/COD (Chemical Oxygen Demand). He stated that he has heard the terms but did not know their meaning.

Strength Based Billing

Mr. Conrad was read the sections of Exhibit 1, a July 3, 1997 memo from Patricia Frazier to Coleman Conrad re: "Sewer Cost of Service Study-Strength Based Billing" (COSS002098) stating the following: "In order to comply with SWRCB Revenue Program Guidelines, we will need to revise our methodology for strength based billing of retail customers . . . Pursuant to SWRCB guidelines, we will need to incorporate a third loading factor – COD/BOD." Ms. Blaskey asked Mr. Conrad his recollection of the document and he could not recall. Mr. Conrad was read Exhibit 2, a July 9, 1997 handwritten memo from Coleman Conrad to David Schlesinger and George Loveland copying Pat Frazier, requesting a recommended action plan (regarding the preceding exhibit) and timeline to implement strength based billing (MWWD-BH0940). Ms. Blaskey asked Mr. Conrad if the one month he provided for a response was typical, and he said it was "standard" for him and a reasonable time to develop a solution. Ms. Blaskey asked Mr. Conrad if the Council had told him not to bring a sewer rate increase proposal forward. He responded that the Council did not want to raise rates, but he did not recall being told not to bring rate increases forward.

Kelco

Ms. Blaskey asked Mr. Conrad about his knowledge of Kelco's involvement with the City's sewer rates. He replied that he heard of Kelco and knew that the company harvested kelp. He stated that he was sure that Kelco generated a lot of sewer waste, and he had spoken to Kelco about addressing its sewer costs. Mr. Conrad would have worked with Schlesinger regarding Kelco's sewer issues and with Loveland regarding Kelco's water issues. He recalled Kelco being opposed to the rate increases and recalled discussions with Kelco about its concern that it would have to leave San Diego if the rates increased (he said he had no way of knowing if Kelco would actually leave). He thought the City should work to come up with a structure that was equitable for everyone. He did not know if Kelco's possible departure from San Diego would influence the City's position on rate increases, and said the possibility had not influenced him. When asked by Ms. Blaskey if he would characterize Kelco's possible departure as a threat, he said he would not. He stated that Kelco's business could not withstand water and sewer rate increases. He said he did not know if Kelco was still in San Diego.

Conclusion

Ms. Blaskey asked Mr. Conrad if he had any concerns regarding improper conduct on the part of any City employees. He said he knew of no improper conduct and did not know of political contributions influencing any elected officials.

WF&G

EXHIBIT 1

CITY OF SAN DIEGO
M E M O R A N D U M

DATE: July 3, 1997
TO: Coleman Conrad, Deputy City Manager
FROM: Patricia T. Frazier, Financial and Technical Services Manager
SUBJECT: Sewer Cost of Service Study-Strength Based Billing

As you are aware, a primary objective of the Sewer Cost of Service study effort is to achieve compliance with the State Water Resource Control Board (SWRCB) proportionate use billing mandates.

Although we are still in the process of reviewing and refining the study, one thing is certain with respect to its impact on the utility. In order to comply with SWRCB Revenue Program Guidelines, we will need to revise our methodology for strength based billing of retail customers.

We currently bill retail customers based on two loading factors: wastewater flow and suspended solids. Pursuant to SWRCB guidelines, we will need to incorporate a third loading factor - COD/BOD. Adding this third factor will require us to:

1. Modify our current two component sewer classification scheme.
2. Reassign all customers to a new classification within the modified scheme.

Over the past several months some preliminary work has been done to prepare for this eventuality, including identification of agencies currently monitoring COD levels for billing purposes. Given the time line for completion of the Cost of Service Study (mid-summer 1997) and the time which may be required to develop, test and deploy the modified system, I strongly recommend that a development/implementation team be formed by Water Department and Metropolitan Wastewater Department management and that the team begin the classification and billing system modification and customer classification efforts necessary to achieve compliance without delay.


PATRICIA T. FRAZIER

PM

RECEIVED

JUL 9 1997

DEPUTY DIRECTOR
Water Utilities/Services

Montano-502

COS002098

WASTEWATER0001287

EXHIBIT 2



THE CITY OF SAN DIEGO

COLEMAN CONRAD

Deputy City Manager

MS 9A • (619) 236-5949 • (619) 236-6067 (FAX)

FAXED
7/16/97

34267 + 83295

7-9-97

MEMO

Dave Schlenger
George Loveland

Pls review attached
7-3-97 memo from
Pat Frasier regarding
strength based billing &
provide a recommended
action plan & timeline
by 8-8-97.

Coleman



CC: Pat Frasier

1 of 2

Btghon

COS 003345-3346

MWWD-BH0940

6-30-05 COS SEC Subpoena

WASTEWATER0001293



CITY OF SAN DIEGO
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Patricia T. Frazier
PATRICIA T. FRAZIER

PM

2 of 2

MWWD-BH0941

6-30-05 COS SEC Subpoena

WASTEWATER0001294